

May 6, 2013

IAASB Technical Director

Dear James,

**Small and Medium Practices (SMP) Committee Response to the Consultation Paper, A Framework for Audit Quality**

**Introduction**

The SMP Committee is pleased to respond to the IAASB on this Consultation Paper (CP).

The SMP Committee is charged with identifying and representing the needs of its constituents and, where applicable, to give consideration to relevant issues pertaining to small- and medium-sized entities (SMEs). The constituents of the SMP Committee are small and medium-sized practices (SMPs) who provide accounting, assurance and business advisory services principally, but not exclusively, to clients who are SMEs. Members of the SMP Committee have substantial experience within the accounting profession, especially in dealing with issues pertaining to SMEs, and are drawn from IFAC member bodies from 17 countries from all regions of the world.

While audit quality is inherently difficult to define let alone determine it is crucial that the global accountancy profession seeks ways of promoting it. Accordingly we applaud the IAASB for issuing this CP as we believe it will help stimulate debate and a sharing of experiences which will go some way towards improving our collective understanding of what it is and how we might improve it.

**General Comments**

We believe the audit quality debate should primarily be made with regard to the public interest. This involves consideration of the costs and benefits to the public, including relative needs, costs and benefits to affected stakeholders, which in reality vary significantly across different stakeholder groups. We therefore commend the IAASB on developing a meaningful and thought-provoking CP. Unfortunately the length of the document could reduce its accessibility to readers.

We note that views on audit quality have traditionally been focused on the audits of public interest entities and so, in welcoming this CP, we appreciate the Board's attempt to recognize SMEs and SMPs. While the thresholds for statutory audit may be increasing in a number of jurisdictions audit quality remains a key concern for the SMP community too. Ultimately the quality of all audits performed (including voluntary audits) reflects on the reputation of the profession as a whole. We therefore believe it is very important to have the SMP community made well aware of and widely involved in this project.

We do appreciate the attempt by the Board to recognize SMEs and SMPs through the inclusion of "Considerations Specific to Audits of Smaller Entities". However, we do have some reservations as to how these considerations have been incorporated as explained under the next section.



Finally, it is unclear what use the IAASB intended for this paper. We presume that the Board does not intend practitioners to use it. We suspect it will primarily be used as a platform for discussion and further research by policy makers, regulators, standard setters, and academics.

## Specific Comments

### Questions in the CP

1. ***Does the Framework cover all of the areas of audit quality that you would expect? If not, what else should be included?***

In general we believe the Framework seems to cover all of the relevant areas of audit quality. However, we do have some suggestions for improving the form and content.

First, we note that in having a section titled “Considerations Specific to Audits of Smaller Entities” (which perhaps ought to be “Considerations Specific to Smaller Entities and Practices” to recognize that it relates to both engagements and firms per the ISAs and ISQC 1) some will inevitably ask what is the definition of small. It would be helpful, therefore, for the paper to refer to IAASB or IFAC definitions. The Glossary in the IAASB Handbook defines “smaller entity”: a simple footnote with a link to this may suffice. Meanwhile the IFAC SMP Committee’s *Guide to Practice Management for Small- and Medium-Sized Practices* includes a definition of SMP. Second, in respect of Section 5.2 it ought to be recognized that smaller entities and smaller practices are not homogenous and so audit quality issues may vary across the population of each. Larger audit firms also of course undertake audits of SMEs. Indeed, the section tends to exclude the considerations pertaining to the audit of medium-sized entities by medium-sized firms. In particular, paragraph 260 is oversimplified, in that there are increasing numbers of audits of SMEs in which there are difficult audit issues, especially related to financial instruments and fair value principles. These complexities significantly impact audit quality, especially for SMPs that lack the resources of larger firms to address them.

Third, we suggest that the outputs summarized at paragraph 27 ought also to refer to some of the less tangible outputs of an audit, outputs which provide some evidence as to audit quality and, while not transparent, benefit the audited entity and its stakeholders. These outputs are likely to be especially relevant in SME audits. At present section 2 concentrates almost exclusively on the reports pertaining to the audit, whether from the audit firm, the audited entity or audit regulators. Section 5.2.2 mentions that the opportunity to provide meaningful business advice is an output common in an SMP audit. We therefore suggest the IAASB consider explaining the nature of such outputs more fully, so as to expand upon the last sentence of paragraph 148,

Finally, while we welcome inclusion of the material in Section 5.2 “Considerations Specific to Audits of Smaller Entities” we fear that audit quality considerations are portrayed as being different or less important in some way. As a result, we are concerned that presenting SMP issues in a separate section may result in SMPs being seen in a far more negative light than might be the case for larger firms and practices. As these are additional considerations to issues presented elsewhere in the paper we wonder whether it would give a more balanced impression to include these together with that material as they are in the ISAs and ISQC 1.



2. ***Does the Framework reflect the appropriate balance in the responsibility for audit quality between the auditor (engagement team and firm), the entity (management and those charged with governance), and other stakeholders? If not, which areas of the Framework should be revised and how?***

In general we believe the Framework seems to cover all of the relevant areas of audit quality and is well balanced. We have, however, made various suggestions for improving the Framework from an SMP/SME perspective above. In addition, we suggest that section 3.4.2, which discusses the role of audit regulators, should include a brief discussion as to how regulators' activities also can (and, where well established, do) influence the quality of the audit. This influence may be both positive and negative, depending on the approach taken and the impact on auditor behaviour. For example, if regulators over-emphasize more administrative matters this may prompt auditors to take a defensive stance which ultimately manifests itself in them focusing on areas such as audit documentation. Any such box ticking mentality may impede rather than enhance the performance of quality audits – especially in SMP audits where a lack of junior audit team members may result in an experienced partner or sole practitioner having to devote disproportionate time to details. We appreciate the fact that audit inspection authorities' roles are noted under "areas to explore", and believe that a more balanced depiction of the potential impact of auditor regulation is warranted.

3. ***How do you intend to use the Framework? Are there changes that need to be made to the form or content of the Framework to maximize its value to you?***

The SMP Committee will continue to promote awareness of the Framework amongst the SMP constituency and encourage SMPs to participate in audit quality debates. We have made some suggestions above that we feel will enhance its presentation of SMP/SME issues. While some SMPs may refer to it, for example in the event a client/audit committee seeks advice as to what might help improve audit quality, we suspect many will not readily use it in its present form. SMPs will likely prefer to see some of the content presented separately in a stand-alone document.

4. ***What are your views on the suggested Areas to Explore? Which, if any, should be given priority and by whom? Are there additional Areas to Explore?***

In general we believe the suggested Areas to Explore appear well articulated. As far as completeness is concerned we suggest they be revisited periodically. In the meantime we wonder whether the following deserve inclusion:

- Improving dialogue between accounting standard setters, audit standard setters, and those involved in inspection activities so as to improve the auditability of reported financial information.
- Investigate the impact of alternative financial reporting frameworks (e.g. IFRS for SMEs) on the quality of SME audits.
- Investigate how the quality of financial reporting may impact on the perception of audit quality.
- Assess the quality of standards (ethics, audit, education, quality control and financial reporting).

From an SMP/SME perspective we believe that areas 2, 4, 6 and 7 should be prioritized.



### **Concluding Comments**

We hope the IAASB finds this letter helpful in enhancing its understanding of audit quality and informing what further steps might be needed. In turn, we are committed to helping the IAASB in whatever way we can to build upon the findings from this consultation and improve the Framework. We look forward to strengthening the dialogue between us.

Please do not hesitate to contact me should you wish to discuss matters raised in this submission.

Sincerely,

A handwritten signature in black ink, appearing to read "Giancarlo Attolini". It is positioned above a solid horizontal line.

Giancarlo Attolini  
Chair, SMP Committee